

Putting development first: concerns about a Pacific free trade agreement

Maureen Penjueli and Wesley Morgan

Coordinator of the Pacific Network on Globalisation (PANG), Suva, Fiji;

PANG's communications officer until December 2009, and is now undertaking a Masters by Research (Political Science) at the University of Melbourne

In the previous issue of *Pacific Economic Bulletin*, Uwe Kaufmann argues that new trade agreements will lead to welfare gains for Pacific islanders—by reducing prices for consumers and reducing production costs for local businesses that rely on imports—and that concerns about ‘adjustments in the production and financial structure’ of Pacific economies will be mitigated by the final design of new trade agreements. Kaufmann (2009) argues that

The IPA [Interim Economic Partnership Agreement] with the European Union and the PACER [Pacific Agreement on Closer Economic Relations] agreement with Australia and New Zealand address not just all of the claims and fears of the Pacific island countries and NGOs in one way or the other, but more importantly address the common barriers to trade identified by the World Trade Organization. (Kaufmann 2009: 173-82)

Kaufmann (2009) states that ‘many non-governmental organisations are antagonistic towards trade agreements involving Pacific island countries, claiming that they will face serious negative consequences if they sign up’. At the Pacific Network on Globalisation, we *are* concerned about the

potential implications of new free trade agreements (FTAs) that include Pacific island countries (PANG 2009). This article responds to Kaufmann’s arguments in favour of Pacific FTAs, focusing specifically on the PACER Plus negotiations between Australia, New Zealand and the Pacific island countries.

A trade agreement for whom?

The Pacific Agreement on Closer Economic Relations (PACER) was not designed to ensure cheaper goods for Pacific islanders or address constraints faced by Pacific businesses. The agreement was designed primarily as a defensive mechanism to ensure Australian and New Zealand exporters and investors would not be disadvantaged if Pacific island countries concluded an FTA with other developed countries.

The then Australian Foreign Minister, Alexander Downer, told Pacific media that ‘the PACER protects Australian interests in the event that Forum Island Countries begin negotiations for a free trade agreement or offer improved market access to another country’ (‘Enduring commitments: an exclusive interview with Australian

Comment

Foreign Minister Alexander Downer', *Pacific Magazine*, [3] [March], <http://www.pacificislands.cc/pm32003/index.php>).

When PACER was tabled in the Australian Parliament for ratification, an accompanying 'national interest analysis' found that

without ratification of PACER, Australia would be denied an enhanced opportunity to negotiate better market access to Pacific markets for Australian business and industry, while any other country, including developed countries like member states of the European Union, could enjoy duty free access to FICs [Forum island countries] for their goods. (DFAT 2002)

More recently, the Australian government has jettisoned talk of PACER Plus being a trade agreement designed to protect its interests and has instead embraced rhetoric about 'regional integration and development'. Australian Trade Minister, Simon Crean, and Parliamentary Secretary for Overseas Development Assistance, Bob McMullan, wrote together in *The Canberra Times* ('International engagement begins in own backyard', Letters to the Editor, 26 August 2008) that PACER Plus would be a 'new, comprehensive, region-wide "trade-plus" free trade and economic integration agreement' that would 'enable the countries in our own neighbourhood to share in the benefits of increased trade and economic growth'.

McMullan toured the region in April 2009 to try to convince Pacific governments that PACER Plus was really about 'reducing poverty' and not about Australian trade interests. He told Radio Australia

[T]his is not about Australia, there's nothing in [PACER Plus] for us, we think it's good for the region. And it is an initiative that we want to extend

because it is beneficial to reduce poverty in the region...It doesn't have any economic significance for us; it's just good for the region as a whole and that's why we're doing it. ('Australian ministers tour Pacific on regional free trade push', Interview with Australian Parliamentary Secretary for Development Assistance, Radio Australia, 1 April 2009, <http://www.radioaustralia.net.au/pacbeat/stories/200904/s2531920.htm>)

In recent years, additional support for a regional FTA between Australia, New Zealand and the Pacific has come from multilateral institutions such as the World Bank and the Asian Development Bank (ADB 2008; Luthria 2009). The intellectual case for a new FTA has rested largely on arguments for the 'welfare-enhancing' effects of tariff reductions and arguments that other elements, such as temporary labour mobility and 'aid-for-trade' resources, could be included in the design of PACER Plus to outweigh the 'negative adjustment costs' for the island countries.

We maintain that this is putting the cart before the horse. Clearly, trade arrangements between the Pacific island countries and Australia and New Zealand can, and should, be dramatically improved but there is no need to negotiate a dangerous FTA to do so. The key question should be: how can trade assist with improving development outcomes for the Pacific? It should not be: how can we make an FTA more palatable?

Tariffs and the revenue consequences of PACER Plus

Few (perhaps other than Kaufmann) argue that there will not be serious adjustment costs for Pacific island countries if they conclude a reciprocal FTA with Australia and New Zealand. A key cost would be a

Comment

dramatic loss in government revenue. As the World Bank's senior economist for the Pacific region, Dr Manjula Luthria, writes: 'it is hard to deny that the Pacific's hesitation to negotiate the PACER Plus agreement has some just cause. After all, tariff revenues comprise upwards of 10% of all government revenue in most islands, and their reduction will leave behind a significant hole in their budgets' (Luthria 2009).

Discussion continues across the region about exactly how much government revenue would be lost if PACER Plus negotiations are concluded and, as Kaufmann points out, there are significant differences between the findings of recent studies into potential revenue losses. While acknowledging that due to these significant differences, 'there is need for further research on the potential tariff revenue losses', Kaufmann (2009) nevertheless argues that 'compared with earlier studies the latest study of tariff revenue losses (Watergall Consulting Limited 2007) suggests that potential revenue losses have been declining significantly'.

The Watergall report in fact indicates that figures contained within it are likely to understate revenue losses—as under

PACER Plus imports from Australia and New Zealand would become more competitive and would gain market share from other tariff-paying import sources (trade diversion from other Southeast Asian countries, for example), thereby increasing the revenue loss.

In any case, the report indicates that, after implementing the Pacific Island Countries Trade Agreement (PICTA), the Economic Partnership Agreement (EPA) and PACER Plus agreements, a number of Pacific island countries will lose more than 20 per cent of their government revenue (Vanuatu, Tonga and the Republic of the Marshall Islands), and others will face dramatic losses as well, such as Kiribati (19 per cent), Samoa (16 per cent) and Tuvalu (14 per cent). These are hardly figures to ease the concerns of Pacific governments struggling to provide social services to growing populations. For many Pacific island countries, the projected revenue losses under PACER Plus equate to a significant proportion of—or exceed—their entire health or education budgets (Table 1).

Clearly, governments in the region can ill afford to lose this much revenue.

Table 1 Government expenditure on health and education and PACER revenue losses (as a percentage of the total budget)

Country	Education	Health	PACER revenue loss
Cook Islands (2005)	13.9	11.3	6
Fiji (2002)	29.4	14.3	3
Kiribati (2005)	14.0	9.3	15
Papua New Guinea (2002)	10.0	5.7	2
Samoa (2005)	22.1	16.7	12
Tonga (2002)	12.9	13.9	19
Vanuatu (2005)	22.7	11.1	18

Sources: Gani, A., 2009. 'Health care financing and health outcomes in Pacific island countries', *Health Policy and Planning*, 24(1):72–81; Oxfam Australia and Oxfam New Zealand, 2009. *PACER Plus and its Alternatives: which way forward for trade and development in the Pacific?*, Oxfam Australia, Melbourne, and Oxfam New Zealand, Auckland.

Comment

Box 1 Introducing a VAT to replace tariff revenue: lessons from Samoa and Tonga

Pacific countries are frequently told that, to avoid revenue losses as a result of trade liberalisation, they should introduce a VAT to meet any shortfall. Samoa, which introduced a value-added goods and services tax (VAGST) and unilaterally reduced tariffs in the late 1990s, is often pointed to as an example of successful, trade-oriented reform. Tonga has followed suit more recently, introducing a consumption tax in 2005 to offset revenue losses on joining the World Trade Organization (WTO), which it did in 2007.

The experience of both countries suggests that this process has been difficult and raises serious questions about the ability of both countries to respond to future revenue losses under PACER Plus.

Samoa introduced its VAGST in 1994—levied at 10 per cent—in anticipation of tariff reform. Then, in 1998, Samoa unilaterally reduced its applied tariff rates and applied to join the WTO. The fall in tariffs saw a significant increase in imports, particularly of food and beverages, adding to Samoa's already considerable trade deficit (Oxfam International 2005). Since then, Samoa has struggled to maintain the revenue needed to pay for essential services and has raised the VAGST twice in the past decade to meet its budget needs (to 12.5 per cent in 2002 and to 15 per cent in 2006). Even with these tax hikes, Samoa continues to struggle to pay for social services and infrastructure projects. In its 2009 budget, for example, Samoa cut 8 per cent and 14.9 per cent, respectively, from the education and health budgets (Government of Samoa., 2009. *2009/2010 Budget Address: Minister of Finance, Hon Niko Lee Hang*, http://www.mof.gov.ws/uploads/budget_address_2009-2010.pdf).

Recent studies indicate that Samoa stands to lose at least 16 per cent of its government revenue on implementing PICTA, the EPA and PACER Plus—the equivalent of almost all its health budget (Watergall Consulting Limited 2007). It is difficult to see how services could be maintained without again raising the VAGST or extending it to new areas (such as health, education and bus and taxi transport).

If the revenue outlook for Samoa (on the introduction of PACER Plus) looks bleak, it looks no better for Tonga. Before 2005, Tonga relied heavily on tariff revenue, with across-the-board tariffs of 25 per cent in place (and additional tariff rates applied to some goods—notably, petroleum 35 per cent, vehicles 45 per cent, foodstuffs 15–25 per cent, alcohol 200 per cent and tobacco 330 per cent). On joining the WTO in 2007, Tonga agreed to bind its tariffs at a lower rate than any other country in the history of the WTO (with the sole exception of Armenia), reducing applied tariffs to a flat rate of 15 per cent, with an across-the-board bound tariff rate of 20 per cent.

To offset revenue losses, Tonga introduced a consumption tax in 2005, levied at 15 per cent. This policy assumption—that tariff revenue would be replaced with a consumption tax—was risky, given problems other countries had faced in implementing a VAT and the fact that Tonga had no fall-back position, having agreed to a bound tariff rate of 20 per cent. Furthermore, Tonga almost certainly faces the prospect of further tariff cuts in future WTO negotiations.

In 2008, Tonga continued with the tax reform required on acceding to the WTO (converting *ad valorem* tariffs of vehicles, fuel, tobacco and alcohol into specific excises, and lowering remaining tariff rates). A 2009 *Country Report* by the IMF found that these changes contributed to a dramatic downturn in Tonga's government revenue, with 20 per cent less government revenue than expected collected in 2008/09 (IMF 2009a). The Tongan government collected P20 million (2 per cent of GDP) less than it budgeted for.

This dramatic fall in revenue has the potential to compound Tonga's external debt situation if the government takes on new loans to meet the shortfall. A joint study completed last year by the IMF and the World Bank (IMF 2009b) indicates that Tonga remains 'at a high risk of debt distress', having taken on a considerable reconstruction loan from the EXIM Bank of China after civil unrest in 2006.

Tonga cannot raise tariffs again (or at least not very far) due to its WTO commitments and it cannot borrow much more given its 'high risk of debt distress'; hence IMF staff have advised the Tongan government to 'carefully prioritise expenditure allocations', including possibly delaying a planned wage increase for the public sector. It also seems likely that Tonga will raise its consumption tax in the future (as Samoa has done). This is especially likely if PACER Plus is implemented as an FTA, for recent studies indicate Tonga will lose at least a further 19 per cent of government revenue in such a scenario (Watergall Consulting Limited 2007). In the event that this much revenue is lost (and given problems with replacing the revenue through the consumption tax), it is hard to see how Tonga could service its external debt and continue to provide social services and pay its public servants.

PANG (2009) has argued that because of lost government revenue due to trade liberalisation, Pacific governments will be forced to cut services to their people or downsize their public sector. Sadly, it looks increasingly likely that this will happen in Tonga. Given the implications of tariff liberalisation for government revenue in Samoa and Tonga, and recent experiences in both countries, the onus is on the Australian and New Zealand governments to indicate how an FTA could be of benefit for countries such as Samoa and Tonga—and the warning for other Pacific states involved in the PACER Plus negotiations is clear.

Comment

Kaufmann (2009) argues that implementing a consumer tax in the form of a value-added tax (VAT) would replace this lost revenue. He writes: 'If implemented wisely, this tax can be effective in offsetting tariff revenue losses. Combined with an excise tax on "sinful" goods, such as alcohol, tobacco and luxury goods, tariff revenue losses can be overcome while serving a social agenda' (Kaufmann 2009:173-82).

There is, however, very little evidence that small and low-income countries have succeeded in replacing revenue lost through the reductions in tariffs. A key study completed by the International Monetary Fund (IMF), which asked the question 'over the last 25 years, have countries actually managed to offset reductions in trade tax revenues by increasing their domestic tax revenues?', found that 'for low income countries, recovery has been far from complete...at best, they have on average recovered no more than around 30 cents of each lost dollar' (Baunsgaard and Keen 2005). Furthermore, the study found that 'there is no systemic evidence that low-income countries with a VAT have recovered more than those without' (Baunsgaard and Keen 2005)—again, hardly advice that would put Pacific governments at ease.

There are recent examples from our region of countries struggling to replace lost tariff revenue. When the Asian Development Bank, as part of conditions for a new loan in the late 1990s, forced Vanuatu to lower tariffs and introduce a VAT, the country suffered massive revenue losses that it took many years to recover from (Oxfam International 2005). Recent findings from Samoa and Tonga also highlight difficulties associated with using a VAT to replace trade taxes (Box 1).

Despite claims that revenue can be replaced through moving to a VAT or through 'prudent financial management', it seems likely that for many Pacific states

revenue losses incurred under PACER Plus will be lasting.

Consumer gains?

Kaufmann (2009) argues that PACER Plus could benefit Pacific consumers through cheaper imported goods, with flow-on benefits to other sectors of the economy (increased disposable income to spend on other goods and services, for example). Experience suggests, however, that even if tariffs are lowered, in many cases exporters and distributors ('middle men') tend to increase their prices almost back to the same level after tariffs are removed and fail to pass on the benefits to consumers.

There are recent examples of this from within our region. When Vanuatu lowered tariffs as part of conditions for a new ADB loan in the late 1990s, benefits were not passed on to consumers. A report commissioned by the UN Development Programme on *Leveraging Trade for Human Development in Vanuatu* (Wagle 2007) found that one of the 'benefits of trade liberalisation—a fall in retail prices of consumer items—is not evident in Vanuatu'.

If PACER Plus is designed as an FTA, Pacific island countries will need to replace lost tariff revenue if they hope to continue to supply services to their people. There are a number of economies of scale in government that very small countries cannot exploit and the cost of government is relatively high when compared with countries with larger populations. If Pacific countries are forced to introduce (or raise) consumer taxes to replace predicted revenue shortfalls, any positive impacts of trade liberalisation on Pacific island countries—including on consumers—will be far less than standard economic modelling suggests. If, for example, a 15 per cent tariff on a wide range of goods is replaced with a 15 per

Comment

cent VAT, the net effect will be very little. Standard economic modelling of the effects of trade liberalisation models the effects of tariff elimination, holding everything else—including other taxes—constant. If, instead, governments replace revenue lost from tariff elimination by raising alternative taxes, this would dramatically undermine the economic gains predicted in that modelling.

Any fall in the price of consumer goods as a result of tariff reductions under PACER Plus is likely to be offset at least partially by increases in consumption taxes (introduced to meet serious government revenue shortfalls). Indeed, for many Pacific island countries, consumption taxes are already imposed at what might be thought of as a 'maximum feasible rate'. To raise taxes further would see the regressive effects of high consumption taxes becoming increasingly pronounced. Further research into the impact of recent tariff reductions, and the consequent introduction of a consumption tax, on domestic prices in Tonga could be useful.

Kaufmann (2009:180) acknowledges that for smaller Pacific island countries, which are heavily reliant on imports, a uniform flat tariff rate and a VAT have roughly similar economic effects. Flat tariffs, however, are much simpler and less costly to administer—with fewer avenues for evasion—than a VAT, and switching to consumer taxes would transfer the administrative burden of collecting taxes to small-business owners and operators in the Pacific (many of whom work only with cash and therefore easily escape the VAT).

A further key point is that Pacific island countries can lower tariffs on a unilateral basis at any time they like—if such a move is deemed to be of benefit to local consumers and producers. This would avoid the dangerous—and irreversible—conditions of an FTA with Australia and New Zealand.

For many Pacific island countries, lowering tariffs further also needs to be considered against maintaining local livelihoods and jobs. Allowing cheaper imports from Australia and New Zealand to gain a greater domestic market share is likely to displace local producers—leading to business closures and job losses. Narsey (2003) predicts that under PACER Plus (if it is designed as a reciprocal FTA) three-quarters of Pacific manufacturing would close, leading to unemployment for thousands of workers (Institute for International Trade 2008:85). Furthermore, some foreign-owned subsidiaries operating in the Pacific are likely to relocate to Australia and New Zealand if tariffs are removed under PACER Plus (and export to the region from there), compounding further the anticipated rise in unemployment and business closures (Narsey 2003).

It is not only current businesses that would be affected, as PACER Plus would radically undermine the policy space available to develop new Pacific businesses—reducing the ability to nurture local businesses through tariff protection, subsidies, investment rules (requiring foreign firms to partner with local firms), government procurement provisions (favouring local employers), and so on.

Finally, PACER Plus is not only about tariffs affecting trade in goods. PANG has a range of other concerns about the potential implications of PACER Plus. For example, Australia and New Zealand are likely to push for an FTA that allows their companies to provide services in the Pacific (including essential services such as health, education and electricity). This could exacerbate existing inequalities in access to services in the Pacific and reduce policy options available to ensure universal access to services. Furthermore, new rules for Australian and New Zealand service providers and investors could also undermine indigenous land

Comment

rights in the region if restrictions on foreign ownership of land are deemed a 'market access restriction' during the PACER Plus negotiations.

Alternatives to a traditional FTA

Contrary to Kaufmann's (2009) claim that PANG is antagonistic towards trade agreements involving the Pacific island countries, we fully support new trading arrangements that help to improve development outcomes for Pacific island countries. We maintain, however, that a WTO-compatible free trade deal would be dangerous—and inappropriate—for the region. We also argue that the template offered by the EPA discussions with

the European Union is inappropriate in the PACER Plus context. Thankfully, arrangements that would genuinely foster regional integration and improve trade opportunities for the island countries are limited only by the political will of the parties involved.

There are a number of ways that the current South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA) could be improved to help Pacific island countries use trade to overcome poverty (Table 2 suggests components that could be included in a 'SPARTECA Plus' type arrangement).¹

The World Bank recently identified two areas of 'comparative advantage' for the Pacific island countries: agriculture and labour (Luthria 2009). It is clear that

Table 2 Components of a 'SPARTECA Plus' trade deal

Investment in trade-related infrastructure (roads, wharves, airports, produce treatment facilities, and so on).

Improvements in regional recognition of qualifications and additional resources for regional training colleges.

Well-designed regional labour mobility schemes, allowing low-skilled workers to work temporarily in Australia and New Zealand.

Improved rules-of-origin requirements for Pacific exports to Australia and New Zealand.

Improvements in Pacific agricultural exports through the removal of quarantine barriers, and expediting the assessment (by Australian and New Zealand quarantine agencies) of new products for Australian and New Zealand markets.

Investment in regional trade facilitation projects (examples include technical projects through the Secretariat of the Pacific Community [SPC] to manage fruit fly in Pacific countries and develop new bilateral quarantine agreements with Australia and New Zealand).

Resources to improve the marketing of Pacific produce and provide better market information to potential Pacific exporters (building on the capabilities of the Pacific Islands Trade and Investment Commission, which has offices in Sydney and Auckland).

Improving the presence of 'fair trade' and 'organic' exports from the Pacific (by supporting the development of regional certifications and helping farmers to overcome barriers to these value-added markets—by reducing costs of certification and marketing).

<h2 style="margin: 0;">Comment</h2>

in both of these areas, a new regional trade agreement could be beneficial; but an FTA is dangerous and wholly unnecessary.

Taking agriculture first, it is true that Pacific agricultural exports are much underdeveloped, especially given the prevalence of productive agricultural systems in the Pacific island countries—for subsistence and cash income—and climate advantages (for tropical fruits and root crops, for example).

A 'SPARTECA Plus' regional trade agreement could open new export pathways for agricultural exports by providing resources and expertise to meet Australian and New Zealand quarantine requirements, and prioritising the assessment of Pacific produce by quarantine agencies. At the moment, Australia is especially slow at assessing the entry of new products (consequently, there is a greater range of 'export pathways' available for fresh produce to enter New Zealand than for the Australian market).²

Regional technical programs (providing expertise in areas such as entomology and plant pathology) could be of great assistance in helping exporters meet the quarantine and labelling requirements for overseas markets. The Regional Fruit Flies Management Project (run through the SPC from 1994 to 1997) made very good progress in developing bilateral quarantine agreements for the export of fresh produce to New Zealand (McGregor 2007).

As well as facilitating new exports, a 'SPARTECA Plus' agreement could help add value to Pacific agricultural exports by helping farmers to sell their produce as 'fair trade' or 'organic' produce—allowing retailers to sell Pacific produce for a premium to discerning consumers in Australia and New Zealand.

The development of 'fair trade' produce could help to bring much needed cash into farming communities and insulate farmers

against future collapses in commodity prices. In Papua New Guinea, for example, smallholder farmers are the backbone of the coffee export industry and, according to recent studies, 'coffee is the main driver of the internal economy...the one that fuels economic activity within the country' (Riedl 2009).³

SPARTECA Plus could also contain commitments to build on the capacity of the Pacific Island Trade and Investment Commission (PITIC) by expanding the organisation's ability to undertake market research on behalf of Pacific exporters and assist with the marketing of 'Pacific' branded products. Developing new marketing for agricultural products as 'fresh from tropical paradise'—building on popular conceptions of the Pacific—could add a premium to exports. The export success of 'Pure Fiji' beauty products is built on such a marketing strategy.

Under a SPARTECA Plus arrangement, new resources could also be allocated to improving key trading infrastructure (such as rural roads, ports and pre-shipment quarantine facilities).

In comparison, designing PACER Plus as an FTA would remove key policy options for developing Pacific agriculture (including seasonal tariff protection and occasional subsidies when prices for island commodities, such as copra, fall) and is likely to promote a greater reliance on food imports and increased competition for local producers from foods produced in Australia and New Zealand. Over time, this would undermine the income and livelihoods of local farmers.

The World Bank argues that, other than agriculture, 'the other main exportable item from the Pacific is semi-skilled and unskilled labour' (Luthria 2009). Again, it is not clear why an FTA is necessary to improve opportunities for Pacific islanders to work overseas. Australia and New

Comment

Zealand are developing temporary labour mobility schemes that allow small numbers of Pacific islanders to fill labour shortages in their horticultural industries. Demand for unskilled labour, however, fluctuates in both countries and a binding commitment to a quota of Pacific island workers as part of an FTA under PACER Plus is extremely unlikely.

The existing schemes are 'market driven' (with no set quotas, as employers determine the size of the annual intake of workers). Other FTAs negotiated by Australia and New Zealand do not offer hopeful precedents for the Pacific, as negotiations have focused on market access for executives, professionals and skilled self-employed contractors who service transnational corporations and meet skills shortages. As a recent study commissioned by the Pacific Islands Forum Secretariat points out, Pacific 'priorities include the free movement of skilled and unskilled labour, however we believe it is unlikely that PACER Plus negotiations will encompass free movement of unskilled labour' (Nathan Associates 2007).

If Pacific island countries negotiate an FTA including trade in services in the hope of gaining labour mobility commitments, they could simply end up with what they already have. That is, they might gain a temporary labour mobility scheme designed to meet labour shortages in Australia and New Zealand (which can be suspended when unemployment rises in those countries) through Mode 4 concessions (with onerous conditions), or a side letter that deals with labour mobility. In return, Pacific island countries might have to liberalise a range of service markets and surrender sovereignty over key areas of national economic policymaking.

Regional labour mobility schemes, improvements in agricultural exports through the removal of quarantine barriers,

investment in infrastructure and plans to expand training colleges and improve regional recognition of qualifications are all key priorities for the Pacific, but clearly an FTA is not the appropriate vehicle with which to pursue these interests.

Conclusion

The push to design PACER Plus as an FTA originates largely from policymakers in Australia and New Zealand (and from supporters at multilateral institutions such as the World Bank and the ADB). Australia and New Zealand have considerable experience negotiating FTAs and stand to gain commercially from PACER Plus. The majority of any increase in trade brought about by PACER Plus will come in the form of an increase in Australian and New Zealand exports to the Pacific island countries—displacing domestic production and imports from other countries and adding further to the considerable trade imbalances faced by many Pacific countries.

Kaufmann (2009) and other proponents of a regional FTA under PACER Plus argue that even if there were to be considerable tariff revenue losses under such a deal, Pacific island countries should simply bear these costs—at least in the short term—until the 'benefits' of an FTA are realised. It is not at all clear, however, that Pacific countries stand to gain much from an FTA with Australia and New Zealand—even in the longer term.

Island countries already have duty-free and quota-free access to Australian and New Zealand markets, and a traditional FTA will not necessarily solve other non-tariff barriers to trade (affecting potential exports of agricultural goods, for example). As Luthria (2009) from the World Bank writes, the 'pain' arising from an FTA could well be permanent

<h2 style="margin: 0;">Comment</h2>

This is where the stark reality of many small states facing preference erosion will need to be faced in bilateral, regional and ultimately multilateral trade liberalisation fora. For many small states this pain is permanent, because they simply do not have the size and location advantages to operationalise their comparative advantage.

Rather than creating additional development components to entice Pacific countries to enter a trade agreement that locks them into this 'stark reality', or finding ways to justify a trade deal designed to meet Australian and New Zealand commercial interests, perhaps a trade agreement should be designed to meet, first and foremost, the needs of the Pacific island countries.

Notes

- ¹ While 'SPARTECA Plus' is put forward here as an alternative to PACER Plus, it is not necessary that a separate and different 'SPARTECA Plus' agreement be negotiated to achieve a flexible, development-oriented trade agreement. The Australian government's recent contention that PACER Plus is not linked to the original PACER means that there is no requirement whatsoever to design PACER Plus as a free trade agreement; the components of a 'SPARTECA Plus' alternative could form the content of PACER Plus itself.
- ² In interviews with the authors, Fijian exporters complained that non-tariff barriers made it especially difficult to export to Australia. Sant Kumar, chairman of the Fiji Fruit and Vegetable Industry Council, explained that it had taken the better part of a decade to have heat-treated pawpaw cleared for entry into Australian markets (nine years longer than it took to gain entry to New Zealand). As Kumar explained: 'trade, trade, trade...all the time we hear that trade is a solution...I tell you how can

there be any trade if there is no market access for our products?' Saten Kumar, operations manager for Mahen's Exports (based in the Sigatoka Valley in central Viti Levu, Fiji), said his company was focusing on exports to New Zealand, as a greater range of fresh produce was covered by bilateral quarantine agreements with New Zealand. Mahen's Exports purchases about F\$20,000 worth of produce from village farmers in the Sigatoka Valley each week, exporting dalo, eggplant, chillies, long beans, okra, curry leaves, dalo leaves (*rourou*), and so on. Fiji's agricultural exports to New Zealand are much greater than to Australia. In 2008, Fiji exported nearly 90,000 tonnes of agricultural produce to New Zealand, valued at F\$48 million. Fiji exported just 15,000 tonnes to Australia, valued at F\$36 million (only F\$15 million if sweet biscuits were excluded).

- ³ At present, Pacific island countries are still developing a regional certification for organic and fair trade produce. A new regional trade agreement could provide resources (and a timeline) for the establishment of such certification. Village farmers often lack the initial capital to gain fair trade or organic certification (costs are often high, requiring assessors to attend the farm site). 'SPARTECA Plus' could remove this market access barrier by providing resources for certification and for the reproduction of 'best practice' models for farmers' cooperatives (cooperatives being more likely to meet certification costs).

References

- Asian Development Bank (ADB), 2008. *Pacific Trade Issues*, Asian Development Bank, Manila.
- Baunsgaard, T. and Keen, M., 2005. *Tax revenue and (or) trade liberalization*, IMF Working Paper WP/05/112, International Monetary Fund, Washington, DC.
- Department of Foreign Affairs and Trade (DFAT), 2002. *National Interest Analysis: Pacific Agreement on Closer Economic*

<h2 style="margin: 0;">Comment</h2>

- Relations (PACER), done at Nauru on 18 August 2001, Department of Foreign Affairs and Trade, Canberra.*
- Gani, A., 2009. 'Health care financing and health outcomes in Pacific island countries', *Health Policy and Planning*, 24(1):72–81.
- Government of Samoa, 2009, 2009/2010 Budget Address: Minister of Finance, Hon Niko Lee Hang, http://www.mof.gov.ws/uploads/budget_address_2009-2010.pdf
- Institute for International Trade, 2008. *Research Study on the Benefits, Challenges and Ways Forward for PACER Plus—final report*, June 2008, Institute for International Trade, University of Adelaide.
- International Monetary Fund (IMF), 2009a. *Tonga: 2009 Article IV consultation*, IMF Country Report No. 09/292, September, International Monetary Fund, Washington, DC.
- , 2009b. *Tonga: joint IMF/World Bank debt sustainability analysis 2009*, International Monetary Fund, Washington, DC.
- Kaufmann, U., 2009. 'Pacific trade liberalisation and tariff revenues', *Pacific Economic Bulletin*, 24(3):173–82.
- Luthria, M., 2009. *PACER Plus*, Pacific Institute for Public Policy, Port Vila, Vanuatu. Available from <http://www.pacificpolicy.org> (accessed 16 November 2009).
- McGregor, A., 2007. 'The export of horticultural and high-value agricultural products from the Pacific islands', *Pacific Economic Bulletin*, 22(3):81–99.
- Narsey, W., 2003. *The Inclusion of Alcohol and Tobacco Products in PICTA*, Report for the Pacific Islands Forum Secretariat, Suva, Fiji Islands.
- Nathan Associates, 2007. *Pacific Regional Trade and Economic Cooperation—joint baseline and gap analysis*, November, Pacific Islands Forum Secretariat, Suva, Fiji Islands.
- Oxfam Australia and Oxfam New Zealand, 2009. *PACER Plus and its Alternatives: which way forward for trade and development in the Pacific?*, Oxfam Australia, Melbourne, and Oxfam New Zealand, Auckland.
- Oxfam International, 2005. *Blood from a stone*, Oxfam International Briefing Note, Oxfam International, London.
- Pacific Network on Globalisation (PANG), 2009. *10 Reasons to challenge the Pacific Agreement on Closer Economic Relations (PACER-Plus)*, Fact Sheet (1), April, Pacific Network on Globalisation, Suva, Fiji Islands.
- Riedl, E., 2009. 'Fair trade: evaluating opportunities for smallholder coffee growers in Papua New Guinea', *Pacific Economic Bulletin*, 24(2):122–40.
- Wagle, S., 2007. *Leveraging Trade for Human Development in Vanuatu—summary of issues*, Asia-Pacific Trade and Investment Initiative, UNDP Regional Centre in Colombo, Sri Lanka.
- Watergall Consulting Limited, 2007. *Responding to the Revenue Consequences of Trade Reforms in the Forum Island Countries*, Final report, September, Watergall Consulting Limited, Port Vila, Vanuatu.